IN THE

ed States Court of Appeals

FOR THE NINTH CIRCUIT

E. TOOK,

Appellant,

vs.

. WESTOVER,

Appellee.

E. TOOK and FLORENCE D. TOOK,

Appellants,

vs.

WESTOVER,

Appellee.

APPELLANTS' OPENING BRIEF.

FISK, ROLSTON, LEVINTHAL & KENT,
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I.

no evidence to support the findings of fact from was drawn the trial court's conclusion that the plain- l not form and carry on the business in question as nership within the meaning of the Internal Revenue

II.

A proper application of the principles, governing the
nation of the validity of a partnership, to the fact
lished by the record, indicates that the conclusion
trial court as to the validity of the partnership is
to law .....

A. The following principles of law govern the det
tion of the validity of the partnership in the
case .....

(1) If a partnership exists under commercial
exists for tax purposes—the tests are th
The ultimate question is whether the par
was a sham or whether there was a real i
carry on the business as a partnership.....

(2) There is no different test to be applied i
mining the validity of a family partnership
applied in testing the validity of a partnersh
strangers .....

(3) There is no distinction between limited
ships and general partnerships for income t
poses, and limited partnerships are recogni
tax purposes .....

(4) A partnership is an organization for the
tion of income to which each partner con
one or both of the ingredients of income-
or services .....

(5) Neither original capital nor services are n
requisites to the validity of a partnership,
test being the reality of intent to carry on t
ness as a partnership.....

III.

Statutes

Textbooks

IN THE

d States Court of Appeals

FOR THE NINTH CIRCUIT

E. Toor,

Appellant,

vs.

Westover,

Appellee.

E. Toor and Florence D. Toor,

Appellants,

vs.

Westover,

Appellee.

PPELLANTS' OPENING BRIEF.

Jurisdiction.

peal involves federal income taxes for the cal-
s 1943, 1944 and 1945 of appellants Herbert E.
Florence D. Toor. The taxes in dispute with
Mr. Toor for those years, amounting to a total
99.29, were paid by Mr. Toor on or about No-
, 1948, under protest after additional assess-
been made by the Commissioner of Internal
R. 7, 9, 14, 17, 22, 25]. Claims for refund were

for the recovery of the alleged overpayment [
Substantially similar assessments were made to
by Florence D. Toor the wife of Herbert E. To
similar action was brought against the Collect
ternal Revenue on account thereof by Herbert
and Florence D. Toor. The two cases involved
issues and were consolidated for hearing before
trict Court. It was stipulated between counse
decision on appeal in the first case, bearing Dist
No. 10461-Y should be applied to and be decis
appeal from the second case bearing District C
10462-Y (p. 515). Jurisdiction was conferre
District Court by 28 U. S. C. A. Sec. 1340. J
were entered on January 11, 1951 (pp. 80-81).
for a new trial were duly filed by plaintiffs o
22, 1951, and orders denying such motions were
February 6, 1951. On April 5, 1951, notices
were filed [R. 82-84] pursuant to the provisi
U. S. C. A. Sec. 1291.

Statement of the Case.

The complaints in the two actions sought the
amounts paid with interest, as the result of
assessments on the income tax of plaintiffs Mr.
Toor, for the years 1943, 1944 and 1945. The
assessments were based first upon the asserti
partnership known as Furniture Guild of Cali
ganized on November 20, 1942, and in which
was general partner, and the Beverly Hills Nati
and Trust Company as trustee of two trusts, t

s was the disallowance of certain deductions
Mr. and Mrs. Toor. However, there is no ap-
this aspect of the case.

Mrs. Toor were divorced in 1948, and as part
perty settlement agreement, it was provided that
would be entitled to receive and retain as his
roperty any income tax refunds, credits or tax
r the years in question [R. 191].

cases were consolidated for trial and the case
he tax paid by Mrs. Toor (Case No. 10462-Y)
tted and decided on the basis of the testimony
involving the tax paid by Mr. Toor (Case No.
[R. 499]. For purposes of argument, we will
ases as one.

l court ruled that the partnership was not valid
rposes and that the Commissioner of Internal
roperly assessed to the plaintiffs the entire in-
e business upon a community basis.

Presented:

ether the limited partnership should have been
for tax purposes for the years 1943, 1944 and

second question is presented in the event the
stion is answered in the affirmative. The trus-
rustee intended to create an irrevocable trust.
by reason of a clerical error, the irrevocability
s inadvertently omitted from the original trust
ts creating the trusts for the children on No-
1942. The parties confirmed this original in-

of correction of the error, and if the later date whether the income taxes of Mr. and Mrs. Toor affected. This question arising as a result of th error, was not ruled upon by the trial court sin answered the first question in the negative.

Statement of Facts.

(Page references are to the printed record

The appellants, Herbert E. Toor and Florence were married in 1926. Domestic difficulties betw developed prior to 1941, and in that year they live together as husband and wife although they to live under the same roof [R. 96]. Their culminated in a divorce in 1948 [R. 95]. T source of difficulty was the lack of sense of valu ness or money on the part of Mrs. Toor and t thrift manner in which she disposed of money [

Because of this difficulty, Mr. Toor in 1941, make provision for their two children, Barbara and Bruce Alan Toor by changing at least one policy to make them direct beneficiaries, and United States bonds monthly in their name [R. early 1942, the situation had crystallized to the po Mr. Toor discussed with his attorney, Max Finl which to get some of the community property control of Mrs. Toor and himself so that th would have some measure of protection in the domestic situation erupted, or in the event somet pened to Mr. Toor. A trust was the natur

) so as not to expire until after the children were
ge and would come into the property themselves
By the terms of the trust agreements all funds
accumulated in the trusts and there could be no
n until the trusts terminated, which was after
en became of age. In discussing the trusts, it
suggested that if a separate trustee were ap-
e might be able to invest those funds in Mr.
siness which was then conducted as a sole pro-
) under the name of Furniture Guild of Cali-
98].

was adopted for the setting up of a trust for
Mr. Fink talked to the Beverly Hills National
Trust Company, and that bank agreed to accept
eship. Arrangements were also made for the
of a limited partnership of the furniture busi-
the bank, as trustee of both trusts, being the
rtner [R. 104]. Prior thereto, Mr. Toor had
cquainted with the bank or its officers except by
; it was not he who suggested the bank as
. 286-287].

he program had been arrived at and tentative
ents made with the bank, Mr. Fink and Mr. Toor
with a tax consultant and certified public ac-
concerning the tax aspects thereof [R. 103-104].

of the trust agreements were drawn in July or
f 1942 [R. 298]. After negotiations with the
some revisions in the trusts resulting therefrom,
rust papers were drawn. These were signed on
20, 1942 by the bank and by Mr. and Mrs.

trusts. $10,500 went into each of the two tru
child, Barbara, was then about twelve years old
other, Bruce, was then about eight years old.
same day, Mr. Toor and the Beverly Hills Natio
and Trust Company executed articles of limited
ship and a verified sworn certificate of limited
ship, which documents were first drafted some t
the original drafts of the trust agreements we
[R. 115-127, 299, 232].

In connection with the trusts, the bank in its
as trustee, filed donee gift tax returns with both
eral government and with the State of Califor
the basis of irrevocable trusts [R. 332-334].

The certificate of limited partnership was file
corded, a certificate of fictitious firm name publ
commercial agencies and the bank with which
ness had its account were notified, insurance pol
changed, premises for the operation of the busi
leased to the partnership by Mr. Toor, employme
ments were executed by the partnership, partners
were set up, and in general, all acts connected
setting up of the business as a partnership were
137-160].

In accordance with the partnership agreement,
transmitted to the new partnership the sum o
as a capital investment for each of the two tru
Toor conveyed to the partnership by bill of sale

each contributed $10,000, making a total capi-
for the partnership of $60,000.

terms of the limited partnership agreement, Mr.
to receive reasonable compensation for his serv-
, after consultation with the bank, was fixed at
oss sales [R. 290, 338, 364, 367]. It was also
by the partnership agreement that profits should
and distributed in proportion to the investments
to each of the trusts, and four-sixths to Mr.
hat Mr. Toor should have full charge and con-
e partnership business and have full power to
all acts necessary or convenient with respect to
rship business that a general partner in a limited
ip could do in accordance with the laws relating
partnerships. The term of the partnership was
il June, 1955; Mr. Toor had the power to ter-
e partnership by giving thirty days' prior written
which event he could purchase the interests of
d partners at book value. Assets had also been
at book value for the purpose of commencing
ership. Proper partnership books were to be
statements were to be prepared annually or more
30-40].

rtnership agreement also provided that the part-
would be retroactive to September 1, 1942. The
r this was that it was originally contemplated

of the partnership was not accomplished until N
20, 1942. This retroactive feature in the agreen
subsequently eliminated by an amendment to the
so that the agreement and action thereunder wo
form to the true situation, and that income earne
the partnership took effect, would not be credite
partnership [R. 315-316, 388, 405-407].

All business thereafter was conducted in the
the partnership [R. 169-172]. The partnership
a fiscal year ending June 30th of each year. Bo
set up and kept on a partnership basis [R. 388-39
The books accurately and honestly reflected ever
action during the life of the partnership; entries w
quate to disclose the relationship of the partners
transactions in the books were in the name of the
ship; there were no subterfuges or kickbacks of
[R. 388-396, 443-445]. The terms of the limited
ship agreement were in all respects adhered to. M
received a reasonable compensation for his servic
upon three percent of gross sales, which comp
was deducted before the computation of net pr
162, 338].

Mr. Toor managed the business as a general
Accountings were rendered to the bank [R. 19
Profits were divided and substantial distributions
proportion to the investments [R. 339-353].

oor, and $21,443.60 to each trust. On or about
10, 1944, $60,000 of the profits were distrib-
,000 to Mr. Toor and $10,000 to each of the
. 339, 343, 344].

e year ending June 30, 1944, the total net profits
artnership, after deducting Mr. Toor's salary,
,380.38, of which sum $91,586.92 was credited
oor's capital account, and the sum of $22,896.37
ital account of each of the trusts. On February
$60,000 was distributed, $40,000 to Mr. Toor
00 to each of the trusts [R. 346-347].

e year ending June 30, 1945, the total net profits
usiness after deducting Mr. Toor's salary was
.65, of which $66,932.43 was credited to the
count of Mr. Toor, and $16,733.11 to the capital
of each of the trusts. On September 6, 1945,
was distributed, of which $20,000 was distrib-
Mr. Toor and $5,000 to each of the trusts [R.

s funds in the hands of the trustee were invested
e to time in accordance with the trustee's discre-
344-350].

, 1946, the partnership distributed securities hav-
st to the partnership of $211,724.03, of which
.61 worth of securities were distributed to Mr.
$36,489.21 worth of securities to each of the

666.66 worth of assets were distributed to Mr. T
$16,666.67 worth of assets was distributed to ea
trusts. Concurrently therewith a corporation wa
to carry on the business of the partnership in
of "Furniture Guild of California, Inc.," capit
$100,000 and each of the partners contributed to
poration their respective shares of the assets of
nership, other than the securities distributed to
stock in the corporation. The balance of the
the partnership, consisting of cash, was distri
each of the partners in proportion on or about Ju
at which time the partnership was terminated
352, 389-395; Ex. 25].

At the time of trial Mr. Toor's son-in-law wa
associated in the business and Mr. Toor stated
and thought the partnership arrangement wo
bring his son into the business [R. 190, 480-481]

The government has disregarded the partnersh
fiscal years for income tax purposes, and has as
additional tax liability against Herbert E. Toor
ence D. Toor based upon the portion of the pro
the partnership received by the two trusts for
years ending June 30, 1943, June 30, 1944 and
1945 respectively.

The facts relating to the issue of the effect of t
error in the execution of the original trust in

CATIONS OF ERRORS:

hat the Court erred in concluding that the parties orm and carry on as a partnership, within the of the Internal Revenue Code, the business the Furniture Guild of California [Conclusions to 6].

he Court erred in making the following findings

he plaintiff, as manager of the marital community entered into two trust agreements [Finding is was erroneous in that the trust agreements ered into by Mr. and Mrs. Toor and funds con- trust were conveyed by both.

he Bank as trustee executed articles of limited ip for sharing in profits [Finding 11]. This neous because the partnership was created for the of the business and contemplated, among other e sharing of profits.

he trustee was authorized to invest only in the of which plaintiff was a partner or principal er, or in government bonds [Finding 13]. This neous in that the trustee also had the power, in iscretion, to invest part or all of the funds in he securities of the United States or the instru- s or states thereof.

was erroneous in that written confirmation of the intention to create irrevocable trusts was executed cember 14, 1943.

(e) Under the articles of partnership, plaintiff full charge and control of the entire business, full power and authority to do any act necessary venient with respect to the business [Finding 16 was erroneous in that the control, power and was limited to partnership purposes only, and wa limited by the express terms of the partnership a and by the provisions of law regarding limited ships.

(f) The creation of the limited partnership in did not in any way change the control which the exercised over the business [Finding 19]. This roneous in that the financial structure and ope the business was changed and plaintiff's control ited by the provisions of the written partnersh ment, by the provisions of law regarding limited ships and by his fiduciary duties as a general par

(g) The creation and the termination of the ship subsequent to the taxable years were merel of the plaintiff [Finding 20]. This was erroneo the partnership was created and terminated in a with the voluntary agreement and independent of the parties.

l of plaintiff's property on which the business
ed on—in brief, the determination of all matters
judgment or management, control of the prop-
disposition and allocation of funds derived from
ess, including amounts to be allocated each year,
exclusively under the domination of the plaintiff
ll intents and purposes, the creation of the part-
nade no change whatever in the manner in which
ness had been conducted before [Finding 21].
erroneous in that the control by the plaintiff was
than that of a general partner in a limited part-
nd was exercised under the limitations and re-
of the written agreement and of the law, and
fiduciary capacity as a general partner, as dis-
d from control for his own benefit only.

o instance appears where the Bank or its repre-
s used independent judgment, and the trustee ex-
one of the rights of partnership, even by way of
Finding 22]. This was erroneous in that the
use independent judgment, did enforce the writ-
ement, did recognize all of its rights as limited
and, under the circumstances, acted in a manner
ould be expected of a limited partner in a part-
omposed of strangers.

ne trustee did not exercise dominion and control
trust corpus in the business and did not influence

in the business, and influenced the conduct of the
ship, and enforced the partnership agreement.

(k) To the extent that capital played a part in
ings of the business, the plaintiff must still be c
to have created the entire business income becau
control over corpus and income and his retenti
many of the attributes of ownership of the tru
in his business [Finding 24]. This was erroneou
the control of plaintiff was that of a general p
a limited partnership and the earnings of the
were created by the business conducted as a pa
plaintiff received a salary as compensation for his
and the bank did contribute capital in proporti
participation in profits to a business which requ
stantial risk capital for its operation.

(l) The entire effect of the establishment of
nership was merely to permit the children of the
to receive a certain amount of the income when
tiff determined that the income was subject to di
rather than diversion to other business determine
[Finding 25]. This was erroneous in that the i
the partnership went into the trusts; all distribut
required by agreement to be and were proport
the ownership of the business; the discretion to
portion of the income in the business was not an
discretion and was a normal and necessary disc

he plaintiff and the trustee did not act with a purpose in setting up the limited partnership 26]. This was erroneous in that there was a purpose" as that phrase is properly used; there lity of intent and a complete absence of sham or e.

ne plaintiff and the trustee did not in good faith join together in the present conduct of the busi- rprise [Finding 27]. This was erroneous in that circumstances and evidence both direct and in- wed a good faith intent to join in the conduct of rise as limited partners.

nat the Court erred in failing to find on all the factual issues presented. These factual issues under Point IB of the Argument.

nat the Court erred in ruling, in effect, that the determining the validity of a family partnership urposes are different from the tests for determin- alidity of such a partnership in ordinary cases ving taxes.

ne Court erred in ruling in effect, that a family artnership is not valid for tax purposes if no nt capital or services are contributed by the lim- ners.

SUMMARY OF ARGUMENT.

I. There is no evidence to support the findin
on which the Court's conclusion as to the invalid
partnership is based.

A. The pertinent findings of fact are
ported by the evidence.

(1) Both direct and indirect evidence
good faith intention to form and carry on
ness as a partnership.

(2) The control of the business given
in the agreement was not complete for all p
it was for partnership purposes only, was
law, and by the agreement, and were th
normally granted a general partner in a lim
nership.

(3) The control exercised by Mr. T
changed by the creation of the partnershi
from the complete freedom of the individua
tor to the fiduciary position of general pa
limitations and responsibilities imposed by
ment and by law. This fiduciary obligation
ognized and respected at all times by the
their conduct.

(4) The partnership was both created a
nated by voluntary agreement of the parti
at arm's length and using independent jud

(5) The bank as trustee did use indepen
ment, availed itself of its rights as a limite

available to it that it was called upon to exercise,
l to act as would be expected under the cir-
ances if this were a limited partnership with
gers.

Mr. Toor's personal services and skill played
portant role in the earning of the business in-
but he received a salary for such services which
ot unreasonable. The capital and organization
e business itself was the major factor in the
ng of the income of the business, and as one-
owners of that capital and organiaztion, each
e trusts must be considered to have earned one-
of the income of the business over and above
Toor's salary.

The provision that Mr. Toor might determine
mes and amounts of distribution of income, did
ve him an arbitrary discretion, but one that had
used reasonably for the benefit of the business.
a common, normal and accepted function of
gement to determine when and how much of
come of the business is to be distributed.

The words "business purpose" should not be
reted to require a benefit to the business. As
rly interpreted, there was a business purpose
e formation of the partnership; there was no
or subterfuge or paper organization; there was
intent to form a partnership and carry on the
ess as such.

The Court failed to find on all the material is-

Court's ruling that the partnership was invali
purposes, is contrary to law.

A. Principles of law applicable:

(1) If a partnership exists under comm
it exists for tax purposes—the tests are the

(2) No different test is applied in deter
validity of a family partnership than
strangers.

(3) No distinction is made between ge
limited partnerships for the tax question
volved.

(4) A partnership is an organization fo
duction of income to which each partner c
capital or services.

(5) Neither original capital nor service
quired for the validity of the partnership.

(6) The desire of a parent to provide fo
dren is a legitimate motive for creating t
partnerships.

(7) The desire to reduce taxes will not
validity of a transaction if that is not the so
and if the transaction is *bona fide*.

B. Other family partnership cases.

C. An evaluation of the facts of the in
in the light of the above stated principl

he clerical error in omitting the irrevocability
m the original trust instruments did not result
income from the partnership to be attributed
ıd Mrs. Toor or justify the disregard of the
of the partnership for tax purposes.

The facts indicate a true intent that the trusts
evocable from the beginning, to wit: November
942, and that the documents originally signed
ıot contain the irrevocability clause all of the
s believed that they did contain.

The instruments executed December 14, 1943
med the original intention of the parties that
rusts be irrevocable and, in any event, should
nsidered to be retroactive to the date the error
red.

Even if the reformatory instruments were not
ıctive in effect, the clerical error was corrected
e the close of the taxable year of the trusts and
r. and Mrs. Toor, and the income from the part-
ip accruing to the trusts in that year is not
ıle to Mr. and Mrs. Toor.

The same government accepted the donee's re-
made shortly after the creation of the trusts, on
revocable basis; the same government, in rene-
ting war contracts, demanded and received some

ARGUMENT.

I.

There Is No Evidence to Support the Fin Fact From Which Was Drawn the Tria Conclusion That the Plaintiff Did Not I Carry on the Business in Question as a ship Within the Meaning of the Internal Code.

A. THE PERTINENT FINDINGS OF FACT A SUPPORTED BY THE EVIDENCE.

(1) Finding 27.

"The plaintiff and the trustee did not in g intend to join together in the present condu business enterprise."

This finding itself is a conclusion drawn by from the other findings of fact [Findings 16, affecting this issue since there is no direct evide ever to support it. The only direct evidence on was that plaintiff and the trustee did in good fa to join together for the present conduct of the enterprise [R. 98, 201, 336-337, 374-376, 484-4

Thus, for example, Mr. Brooks, the represe the trustee bank, who conducted the negotiation in answer to the Court's questions, as follows [R

"The Court: Was there any understand time that you entered into this agreement

e Court: In other words, you understood that, ct to the limited rights you had in the partner- you were actually entering into this partnership, r as those particular trusts were concerned?

e Witness: That is correct.

e Court: And you were to derive whatever its came to the trusts?

e Witness: That is correct. In a fiduciary ity."

ord is quite clear that there was no understand- than the agreement executed by the parties in , dealing at arm's length and using independent and carried out by them to the last letter. s no agreement between Mr. Toor and his chil- rding the disposition of the trust fund at the on of the trusts [R. 201] and it was not even that the bank was a party to any covert agree-

disputed and uncontradicted testimony of un- l persons may not arbitrarily be disregarded by finder. (*Lawton v. Commissioner* (6th Cir.), 380.)

ll hereinafter further point out in detail that in- concerns all of the indirect evidence from which of the parties may be inferred there is no evi- support a finding that the partnership here con-

(2) Finding 16.

"Under the articles of partnership, plaintif
full charge and control of the entire bus
had full power and authority to do any act
or convenient with respect to the business.'

This finding is not justified by the evidence.
dence shows that as a general partner, Mr. Too
charge and control of the business for *partner*
poses only. Likewise, he had full power and
to do any act necessary or convenient with resp
business *only for partnership purposes*. We s
inafter discuss the distinction between the powe
agement for personal purposes as compared
power of management in a representative or
capacity for the benefit of others. In this case,
was given for the benefit of the partnership of
trusts were part owners. Such powers could no
arbitrarily. As a matter of fact the powers giv
agreement were what a general partner would h
out the agreement.

(3) Findings 19 and 21.

"19. The creation of the limited partn
this case did not in any way change the cont
the plaintiff exercised over the business.

"21. The control of the business incom
manner of its allocation, the salaries to be
by the plaintiff and the employees, the amo
paid for the rental of plaintiff's property
the business was carried on—in brief, the d

· the domination of the plaintiff that, to all in- and purposes, the creation of the partnership no change whatever in the manner in which the ess had been conducted before."

indings are also without support in the record. findings are basically similar, the same evidence scussed in connection with both of them.

ese findings first of all ignore the fact that the a general partner in a limited partnership does m that of an individual proprietor. The control Toor previously had as an individual proprietor limited by his fiduciary obligations as a partner e specific limitations prescribed by law (see Secs. d 15510 of the Corporations Code of California the Appendix hereto). The limitations enunci- e statute are not meaningless.

ese findings also ignore the fact that the control was given and exercised was simply that of a artner in an ordinary limited partnership. Find- hen analyzed, merely amounts to a finding that ess was conducted as a limited partnership Toor having the powers of management of a artner. There is nothing in this that could sup- nclusion that the partnership was not a real one was invalid for tax purposes, unless a limited ip created with gift capital could not be recog- tax purposes. As hereinafter pointed out, this is w. It is extremely significant that neither this or any other finding states that Mr. Toor was

(c) These findings further ignore the diffe
tween control primarily for his own benefit, and
trol exercisable for the benefit of others—in this
the benefit of the partnership of which the trusts
third owners.

See:

Armstrong v. Commissioner (10th Cir., 1
F. 2d 700, and cases cited therein at p.

Greenberger v. Commissioner (7th Cir., 1
F. 2d 990;

Cf. Thomas v. Feldman (5th Cir., 1946
2d 488, aff'd in *Feldman v. Thomas,* 34
R. 1631.

Whatever powers of management Mr. Toor ha
eral partner, he could not exercise them for his
advantage, but had to act for the benefit of the pa
with a proportionate part of the gains going to t
partners. He was neither the beneficial owne
corpus nor the recipient of income therefrom.

(d) These findings further ignore the evidenc
business was at all times conducted as a true a
partnership, which evidence also demonstrated
parties truly intended to enter into the partner
bona fide business relationship.

(1) A written agreement was executed; a b

books were set up and properly kept according
usiness practice for a limited partnership, etc.
60, 338-396, 439, 443]. As far as everyone was
, the business was operated as a partnership [R.

ere is no evidence that Mr. Toor ever did any-
lerogation of the agreement or of the rights of
l partners.

countings were regularly furnished the bank;
l distribution of profits were made; Mr. Toor
with the bank as to his compensation and kept
nformed of the conduct of the business [R. 194,
364, 367, 339-353, 294].

rticularly significant was the conduct of the
the handling of the renegotiation problem which
h respect to sales made to the United States
ing the taxable years in question. A change in
gotiation Act of 1943 increased the amount of
from negotiation for the fiscal year ending
1943, of persons, firms or corporations whose
ar ended after June 30, 1943. Since the partner-
al year ended June 30, 1943, it could not take
of this increased exemption. If the partnership
in effect, Mr. Toor could have taken advantage
creased exemption since his taxable year ended
31. When confronted with this problem, Mr.

resulted in the requirement that the partnersh
a substantial sum to the government.

(5) There was no mere paper allocation of i
indicated in the case of *Commissioner v. Tower,*
280, 66 Sup. Ct. 532, 91 L. Ed. 670, 164 A. L.
There were no rebates or kickbacks from the i
the partnership allocated to the trusts, none of it
for the benefit of the trustors nor was it available
The income was not used to help support the ch
189). All distributions were made in proportion
ership (pp. 339, 353). The full ownership of t
invested in the partnership and the income there
at all times in the trustee. All benefits accrui
trusts actually went into the trusts. In this re
trial court commented as follows [R. 500]:

> "I will say this for you: I intimated a p
> finding of fact on one point, and I will in
> you another prospective finding of fact, wh
> your advantage, and that is this: that the
> shows clearly that the estate, the partne
> spected at all times the rights and interes
> trusts, and at no time was there any attem
> prive these children of the benefits coming t
>
> The only thing that may appear in the
> far is the fact there may be undistribu
> which, of course, it is within the right of a
> ship or corporation to distribute at a partic
> In that respect we do not have a paper org
> If it were paper it would have accumulated
> good money of the United States in the tru
> of those children over this period of years.

(4) Finding 20.

he creation and the termination of the partner-
subsequent to the taxable years were merely the
of the plaintiff."

was no evidence to justify such a finding. The
rtnership was created by a valid and voluntary
t between Mr. Toor and the Beverly Hills
Bank and Trust Company, for a valuable con-
. The consent of each party was freely and vol-
given not only to the creation but also to the
on of the partnership. The bank investigated
and his business prior to becoming a limited
and gave the matter the same consideration as
in making any other investment as a trustee
rust [R. 336, 337, 374]. The terms of the trust
its and partnership agreement were worked out
he parties, the bank requiring provisions therein
ry to it and refusing to accept the documents in
as proposed originally by Mr. Toor's attorney.
had not dealt with the bank or even met its
rior to negotiating with them for the trusts and
ip. [R. 304, 286-287].

nk was also consulted and its agreement was re-
nd obtained for the termination of the partner-
e distribution of the assets and investment in the
on which succeeded to the business of the part-
The bank did not feel compelled to make the in-
in the successor corporation, and considered the

(5) Findings 22 and 23.

"22. No instance appears where the Ba representatives used independent judgment gested any action other than that propose plaintiff. The trustee exercised none of t of partnership even by way of advice.

"23. The trustee did not exercise dom control over the trust corpus in the busines not influence the conduct of the partnersh disposition of its income."

Both of these findings are refuted by the same The evidence shows that the bank realized th actually entering into the partnership and that derive whatever benefits came to the trusts fro eration of the business [R. 376]. After the of the partnership, Mr. Toor kept the bank inf the conduct of the business and consulted with officers from time to time [R. 194, 294]. The cussed with Mr. Toor the fixing of Mr. Toor's sation [R. 290, 338, 364, 367].

The bank received the annual accountings, v them and felt satisfied. [R. 194, 338, 368, 375- bank received its proportionate share of all dis [R. 339-353].

It was recognized that under the limited pa laws of the State of California, the limited par not be active in the management and control of ness. (California Corporations Code, Sec. 155 bank recognized that it had rights under the

nvestigation of the honesty, integrity and com-
f Mr. Toor, and certainly nothing thereafter
that any further investigation was necessary.
felt, based upon the reports that it received,
ity of Mr. Toor and the obvious success of the
that the management of the business was in
ls, that the trusts were getting everything due
none of their rights were in any way violated
368, 374-376]. This particular issue was sum-
by the questions of the Court itself at the con-
the testimony of Mr. Brooks [R. 375-376]:

he Court: Just one question. At all times you
felt and known that you have certain rights as
ited partner, whether they are defined in the in-
nent or whether they are defined by law?

ne Witness: I did. We recognized that.

ne Court: You recognized that?

ne Witness: Yes.

ne Court: You have not exercised those rights
use you have not felt called upon to exercise
?

ne Witness: That is correct.

ne Court: You felt all the time, in relation to
business, the integrity of Mr. Toor, the reports
received, that the management was in safe hands
nothing was going on that would warrant your
king that the trusts were being deprived of what
coming to them, or that any of the assets of the
nership had been diverted to channels not auth-
d by the agreement or by law? Is that not
?

of any limited partner who was a stranger. unusual to have a limited partner with very lit edge of the business. In this case, the business standingly successful, the limited partners we everything they were entitled to and it was ob none of their rights were being violated. It wo expected that the limited partner, even if a would attempt to impose his judgment on that o eral partner even by way of advice.

Even if the bank had done nothing, to say tha had not influenced the conduct of the partnersh disposition of its income is somewhat like sayi contract does not influence the conduct of th because there are no breaches of the contract an based thereon; it is also akin to saying that a not influence or affect the actions of the peop to it because there are no violations and no pr therefor.

(6) Finding 24.

> "The nature of the business was such plaintiff's personal services, business judgm skill played an important role in the earni business income. But to the extent that cap a part, because of his control over corpus a and his retention of so many of the att ownership of the trust corpus in his bus plaintiff must still be considered to have c entire business income."

Mr. Toor's personal services were, of cours tant to the business since he was the sole genera

ultation with the bank. There is no finding alary was unreasonable. With respect to this e note the following:

r. Toor received as salary, $11,972.83 for the th period from November 20, 1942 to June 30, 138.22 for the fiscal year 1944, and $20,579.47 cal year 1945. [Ex. O; R. 162, 393].

Ir. Toor and Mr. Brooks testified the salary was [R. 161-162, 290, 338].

or the years 1937-1940, Mr. Toor derived from ss an average annual earning of $14,164, which oth compensation for his personal efforts and . 339].

Ir. Toor testified that on that same percentage robably would have made $25,000 per year for le years in question, had it not been for the nt work they were doing [R. 276-277].

Ir. Toor had previously managed another s an employee with his compensation based on 3% of gross sales [R. 161]. Mr. Toor also e could have obtained a competent executive to his duties for the same rate of compensation

he salary was fixed in 1942 when the amounts y Mr. Toor by reason thereof were considered compensation for such an executive in an ordi- nercial venture.

he business was not a one-man business, nor a

was ten or eleven salesmen. In addition, there w
hundred or more production workers plus su
employees and office staff [R. 163]. There was
manager, Mr. Coyle, who was a sort of general
in addition to supervising the office, he took c
great many things including purchasing and su
of sales when Mr. Toor was not there. There
a production manager, Mr. Parker, who was in
charge of production and production employees
were also foremen in charge of each division of
[R. 164].

Mr. Toor was away from Los Angeles frequ
ing this period on various trips. While he was a
Coyle and Mr. Parker operated the business [R.
Mr. Coyle and Mr. Parker in salary and bo
earned $10,000 a year [R. 167]. Important
were generally arrived at after a conference
other executives [R. 290-291, 216-217, 238, 2

The major income producing factor during th
was the organization, inventory and equipment
partnership owned and paid for. This was pa
true during the war years when the increase in
business and profits realized was due to pur
the United States Navy. These purchases wer
sults of making acceptable bids and being able t
to meet the orders. The figures for the bids we
worked out by Mr. Coyle and Mr. Parker alth
Toor would pass on them. Once the bids were
and orders received, it would be largely a

upon analyzing this finding, we find that it is
e conclusion as to the ultimate result reached.
no finding as to the extent of control or that
was any greater than would be the case of a
rtner in a limited partnership with strangers.
his finding thus uses the end result itself (the
ion of the invalidity of the partnership) as the
arriving at the result, and skips over the in-
and necessary determination of the reality of
to carry on as a partnership. Thus, this find-
ence says: Although income must be taxed to
rns it, we are going to disregard the fact that
was paid a reasonable salary for his services
e him with earning all of the income of the
p business because the partnership is invalid
rposes; now, since Mr. Toor must be considered
all of the partnership business earnings, and
me must be taxed to he who earns it, obviously
rship is invalid for tax purposes. It is sub-
t this is the only logical analysis of the finding
pointed out, it is not the law that the control
nd exercised by a general partner in a limited
p is sufficient to render the partnership invalid
urposes or make the income chargeable to the
rtner merely because a family relationship ex-

: *Lamb v. Smith,* 3rd Cir. 1950, 183 F. 2d
938;

eenberger v. Commissioner, 7th Cir. 1949, 177

Flandrick v. U. S. (Dist. Ct. So. Calif. 1951), cited in Prentice Hall Par. 725

Cf. Harris v. Commissioner, 9th Cir. 19 2d 444 (rev'g 10 T. C. 818).

In this connection the Court in *Greenberger v. sioner, supra,* at p. 994 commented:

"It is true the court in Tower stated, at page 289, 66 S. Ct. at page 537, 'The iss earned the income,' but the court also st issue depends on whether this husband really intended to carry on business as a pa If the partnership in the instant case was as we think it was, the income earned was t partnership and not that of petitioner. titioner undoubtedly was the predominating the conduct and management of the bus Commissioner overlooks the fact that the ship paid him a salary of $45,000 per annu each of the taxable years for his services ered."

(7) Finding 25.

"The entire effect of the establishmen partnership was merely to permit the child plaintiff to receive a certain amount of t when the plaintiff determined that the in subject to distribution rather than diversio business determined by him."

This finding, as is indicated by its own lan merely a conclusion. It is respectfully submitte

up to in all respects; it disregards the fact that
; intended to form a partnership and carry on
ss as such, and that they did so; it disregards
hat the control over the business and income
y Mr. Toor was different under the partnership
s as an individual proprietor; it disregards the
he income was not under the sole control of Mr.
would be if he were the sole owner of the busi-
could only use it for business purposes which
portionately benefit the limited partners, and he
distribute it unless proportionate distribution
to the limited partners. Furthermore, though
nd amount of distribution of profits was at Mr.
cretion, this was not an arbitrary discretion, if
tion was exercised arbitrarily, the bank as a
rtner had an appropriate remedy in the courts
Limited Partnership Law.

e: *Greenberger v. Commissioner,* (7 Cir. 1949)
177 F. 2d 990, 993.

t that the finding was intended to be limited to
that Mr. Toor could determine the amounts and
distributions of profits. Here again, we have
provision which in no way would tend to sup-
conclusion that the partnership was sham.

lained by Mr. Toor, there are times when the
e best plowed back into new equipment or ex-
nd there are other times when the profits can be
l; certainly it is the management of the business
uld determine, from the point of view of the

such as we have here, whether it be corporate
wise, to retain substantial reserves from pr
business purposes, the amount of which will v
time to time, and which amounts are left to the
of such management. As a matter of fact, Mr.
plained that the provision was taken from a for
ited partnership agreement that he was generally
that time [R. 323].

We note that it was particularly important
the management have the determination of v
how much of the profits to distribute. The bus
in the process of expansion; due to war condi
ventories had been substantially reduced and res
to be set up to cover increased inventory req
when normal times returned; large capital dema
be necessitated by sudden government orders, t
of which could not be anticipated; that the no
and downs of the furniture business were co
exaggerated by the uncertainty of war conditi
note further that before the partnership was c
Mr. Toor had left much of the profits in the
substantially restricting his drawings [R. 411,
165, 497].

Furthermore, Mr. Toor could not derive any
benefit from allowing profits to remain in the
other than the gain he would share with the lim
ners from the resulting benefits to the busin
could not use the funds for personal purposes a
would have no motive for leaving the funds in

efit to the business in permitting profits to re-
ein, it was to the advantage of the trusts that
one rather than having the trusts invest these
government securities at a much smaller re-
pointed out by the Trial Court, the fact that
did not accumulate idle funds was an indica-
the partnership was *not* a paper organization

(8) Finding 26.

he plaintiff and the trustee did not act with a
ess purpose in setting up the limited partner-
'

e Trial Court misinterpreted "business pur-
requiring a business benefit.

Culbertson opinion, the ultimate question to be
the family partnership cases was stated to be
'the parties in good faith *and* acting with a
urpose intended to join together in the present
f the enterprise." (Emphasis added.) The
rt, in this finding, has evidently accepted the
nt's contention that a business purpose, as thus
ns a benefit to the business. Such interpreta-
oneous. To thus interpret the phrase would be
ntrary to the substance of the *Culbertson* ruling,
l make one factor, the absence of a business
nclusive. It is submitted that the words "busi-
se" as used in the *Culbertson* opinion may logi-
terpreted only as referring to the reality of the
arry on the basis as a partnership, and to share

Thus, in the case of *Commissioner v. Tower*, 3
280, 66 S. Ct. 532, 90 L. Ed. 670, 164 A. L.
the Court used these words:

> "When the existence of a limited partne
> rangement is challenged by outsiders, the
> arises whether the partners really and truly
> to join together *for the purpose of carrying*
> *ness and sharing in the profits or losses*
> (Emphasis added.)

It was this statement which the Supreme Cou
Culbertson case, was reaffirming when it used th
in question.

Accordingly, in a subsequent portion of the *C*
opinion, we find the following language (337 U
69 Sup. Ct. 1215):

> "If, upon a consideration of all the facts, it
> that the partners joined together in good
> conduct a business, having agreed that the
> or capital to be contributed presently by ea
> such value to the partnership that the co
> should participate in the distribution of pro
> *is sufficient.*" (Emphasis added.)

This is the interpretation taken by the Appella
in applying the *Culbertson* decision. Thus, in
Commissioner of Internal Revenue (6th Cir., 19
F. 2d 246, 254, it is stated:

> "The test, of course, is not whether there
> or obligation on the part of a business man
> his wife and children partners in his bus

rtnerships, cannot be recognized for tax pur-
re there was no contribution of original capital
s. This is not the law.

mb v. Smith (3rd Cir., 1950), 183 F. 2d 938;
eenberger v. Commissioner, 177 F. 2d 990;
eodore T. Stern, 15 T. C. 521;
n A. Morris v. Commissioner, 13 T. C. 1020;
ndrick v. United States (Dist. Ct. So. Calif.,
May 15, 1951), cited in Prentice Hall, Par.
72515.

e also *Harris v. Commissioner* (9th Cir.), 175
(rev'g 10 T. C. 818), where the Circuit Court
he Tax Court which had held a family partner-
lid, the children contributing neither original
r services. The case was remanded for further
ion in conformity with the *Culbertson* case. If
s benefit were a vital requirement, the Circuit
that case could readily have affirmed the Tax

properly interpreted, the evidence demonstrates
s purpose in that there was a reality of intent
ne partnership and carry on the business as such.
) We have already commented upon the conduct
ne business as a true partnership as indicating
eality of the intent of the parties. In addition,

tributed to the trustee without any strings
Mr. Toor received a salary for his services;
trol was circumscribed by law and by his
character as general partner; his relationsh
corpus of the trusts in the partnership an
come therefrom was changed—he could no
it or avail himself of it for his own purpos

(2) The prime moving purpose in the cr
the trusts was not a mere tax saving devi
prime initiating factor was the desire to ma
rate, independent provision for the childr
result of Mr. Toor's domestic difficulties
spendthrift habits of his wife. It was onl
that the trust invest in Mr. Toor's busine
was a successful one. Naturally, as the pro
gressed, the tax aspects were considered.
tax advantage would accrue was certainly
unwelcome *additional* benefit to be derived
plan. It is settled that the desire to reduc
taxes will not defeat the validity of the tr
so long as it is not entered into for the sole
of saving taxes.

Chisholm v. Commissioner, 79 F. 2d 14;
Ramsey v. Curry (Dist. Ct., Iowa), 88 F
967.

(3) Additional factors indicating the real
intent of the parties:

(a) Mr. Toor had previously operated the
as a limited partnership in 1935 with his

tion of the partnership for a contribution of
0 plus a promise of $2500 more [R. 93, Ex. 1].

) Mr. Toor had previously made gifts to his
ren and subsequent to the formation of the part-
ip continued to make substantial gifts [R. 190].

) In the creation of the partnership, Mr. Toor
definitely depriving himself of that portion of
ncome derived from the business which belonged
e trusts. This was a substantial practical de-
tion in this case. Mr. Toor was a comparatively
g man; his future needs might be very substan-
nd not adequately taken care of by his earnings;
as not a wealthy man, having severly restricted
mount of his drawings and his manner of living
at he could let the profits ride and develop the
ess [R. 93, 96, 165]. He did not have adequate
ves so that he could feel secure that he would
n the future need the corpus or income belong-
o the trusts. Furthermore, the corpus and in-
of the trusts would go to the children when
became of age regardless of the situation that
t develop between himself and the children dur-
he interim. Thus, for example, he would have
ay of preventing the children from turning back
y to Mrs. Toor after they became of age [R.
. We note in addition that the partnership was
ed during the early part of the war when busi-
conditions and future prospects were particularly
rtain. The government orders were about to

B. THE COURT ERRED IN FAILING TO F
ALL THE MATERIAL ISSUES PRESENT

The evidence as heretofore discussed in detail,
that all the following facts should have been fou
Court. Each of these facts are material to the
determination of the reality of the partnership
without contradiction in the record:

(1) That the limited partnership agreer
entered into in accordance with the laws of
of California and in accordance with the exp
visions of formal documents.

(2) That the trustee at all times after
into the partnership agreement owned an i
the business and exercised rights of owner
respect thereto, including receipts of princip
come therefrom, the receipt and examination
ments of operation, and advising with th
partner.

(3) As a general partner, Herbert E.
full charge and control of the entire bus
partnership purposes only; the Bank was at
entitled to exercise the attributes of owne
the rights of a limited partner with respe
partnership business and its assets, and to
proportionate share of profits as fixed by

) That the business was at all times in question
ted as a limited partnership, and in accordance
the partnership agreement.

) That the contribution of capital played an
rtant role in the earning of the business income;
the Bank contributed $20,000 in capital and
ert E. Toor contributed $40,000 of the total
al of $60,000; that the sharing of profits was
oportion to the capital contribution.

) That in addition to his proportionate share of
profits, Herbert E. Toor received a substantial
y for his services to the business, which salary
not unreasonable.

) That the partnership effected a substantial
ge in the economic relation of plaintiffs and their
ren to the income in question.

) That Herbert E. Toor neither had the power
r ever made a distribution of profits to himself
out making a proportionate distribution to the
s.

) The partnership and all parties at all times
cted the rights and interests of the trusts, and
time was there any attempt to deprive the trusts
e children of the benefits coming to them. None
e parties ever did anything in derogation of the

(10) Once the partnership was establish
the benefits that could go into the trusts actu
into the trusts.

(11) Neither of the plaintiffs could or d
from the income earned by and attributed to t

(12) There was no understanding that
and partnership agreements were not to b
out in strict accordance with the provisions
there is no evidence of bad faith on the pa
of the parties.

(13) The parties intended to join togethe
on a business and share in the profits and
partners.

(14) That the partners joined together
faith to conduct a business, having agreed
capital to be contributed presently by each i
value to the partnership that the contribut
participate in the distribution of profits.

II.

r Application of the Principles, Governing Determination of the Validity of a Partner- to the Facts Established by the Record, ates That the Conclusion of the Trial Court the Validity of the Partnership Is Contrary aw.

FOLLOWING PRINCIPLES OF LAW GOVERN DETERMINATION OF THE VALIDITY OF PARTNERSHIP IN THE INSTANT CASE.

artnership Exists Under Commercial Law, It Exists x Purposes—the Tests Are the Same. The Ultimate on Is Whether the Partnership Was a Sham or ıer There Was a Real Intent to Carry on the Busi- s a Partnership.

mmissioner v. Tower (1946), 327 U. S. 280, 66 Sup. Ct. 532, 90 L. Ed. 670, 164 A. L. R. 1135;

mmissioner v. Culbertson (1949), 337 U. S. 733, 69 Sup. Ct. 1210, 93 L. Ed. 1659;

ısburg v. Arnold (5th Cir., 1950), 185 F. 2d 913.

connection, we note particularly the following in the concurring opinion of Mr. Justice Frank- the *Culbertson* case (337 U. S. 753, 69 Sup. Ct.

seems to me important, therefore, to make

a virtue that they have not for the sake of tax men and women may appear in a guise w gimlet eye of the tax court is entitled to pie should leave no doubt in the minds of the Ta of the Courts of Appeals, of the Treasur the bar that the essential holding of the To is that there is 'no reason' why the 'genera which the existence of a partnership is de 'should not apply in tax cases where the go challenges the existence of a partnership for poses.' "

In further referring to the *Tower* case, Mr Frankfurter also states (337 U. S. 750, 69 Sup. C

"In short, the opinion did not say that fam nerships are not to be regarded as partner income-tax purposes even though they be commercial partnerships; the opinion did announce hobbling presumptions under the tax law against such partnerships."

It is submitted that the ordinary commercial of the validity of a partnership are clearly met stant case.

(2) There Is No Different Test to Be Applied in ing the Validity of a Family Partnership Than in Testing the Validity of a Partnership With

As stated in the *Culbertson* case, the "existen family relationship does not create a status wh determines tax questions, but is simply a war things may not be what they seem."

Code so as virtually to ban partnerships com-
of the members of an intimate family group."
phasis added.)

ubmitted that the Trial Court here has taken a
ip that would have been held valid if composed
ers, and ruled in effect that it was sham because
nposed of the members of a family group.

Is No Distinction Between Limited Partnerships
eneral Partnerships for Income Tax Purposes, and
d Partnerships Are Recognized for Tax Purposes.

eenberger v. Commissioner (7th Cir., 1949),
177 F. 2d 990;

mb v. Smith (3rd Cir., 1950), 183 F. 2d 938.

o Regulations 111, Sec. 29.3797.5 (providing a
artnership is classified as a general partnership
urposes).

tnership Is an Organization for the Production of
e to Which Each Partner Contributes One or Both
Ingredients of Income—Capital or Services.

mmissioner of Internal Revenue v. Culbertson,
supra.

er Original Capital nor Services Are Necessary
sites to the Validity of a Partnership, the True Test
the Reality of Intent to Carry on the Business as

(6) The Desire of a Parent to Provide for His C
a Lawful and Legitimate Motive for Creating T
Partnerships.

Armstrong v. Commissioner (10th Cir
143 F. 2d 700;

Thomas v. Feldman (5th Cir., 1946), 1
488.

(7) The Desire to Reduce Taxes Will Not Defeat th
of a Transaction so Long as the Transaction
Fide and Is Not Entered Into for the Sole
Saving Taxes.

Chisholm v. Commissioner, 79 F. 2d 14.

B. OTHER FAMILY PARTNERSHIP CA

It would serve little purpose to review at l
many cases applying the principles set out in the
son case. However, we respectfully invite th
attention to the case of *Greenberger v. Commissi*
Cir., 1949), 177 F. 2d 990. The facts in that
comparable and the observations in the opinion
ticularly pertinent to the facts of the instant cas

In that case, the taxpayer was the main stock
a corporation which derived practically all of i
from commissions earned on sales. Prior to th
years in question, the taxpayer made a valid gi
of the corporation stock to his wife, and later the
and his wife created irrevocable trusts for the

as formed with the taxpayer as general partner
wife and the trusts as limited partners. Con-
pital was $10,000. Profits for the years in ques-
$139,000 and $140,000 respectively. The Com-
attacked the validity of the partnership and the
t found that no valid partnership existed for
purposes. The Seventh Circuit Court reversed
Court and found that a valid partnership did

x Court had found that capital was not a mate-
e producing factor in the operation of the busi-
this respect, the Seventh Circuit Court observed
s true that the capital invested in the partnership
pective parties was not large, but the point was
had decided it was sufficient for the needs of
ss in connection with the available income which
rship had. The Tax Court had also found that
nd the trustees did not perform any services for
ess. The Appellate Court observed that the
of the lack of services and the fact that capital
material income producing factor, indicated at
or in emphasis, and that the predominant factor
ood faith and legitimate purpose of the parties
g the partnership.

espect to the government's contention that the
by the rendition of personal services, was re-

the business as a partnership. If the partne
bona fide the income earned was that of the p
and not that of the taxpayer. *The Appellate C*
pointed out that while the taxpayer was undou
predominant force in the conduct and managem
business, the Commissioner had overlooked the
the partnership paid him a salary for his ser
dered during the taxable years.

The Appellate Court also distinguished the *T*
Lusthaus decisions by pointing out that in th
there was a mere paper allocation of income, w
the case in question, the parents retained no
or control over the property donated and the inc
the trust property had been received and invest
respective trustees in accordance with their tru
tions. It was also stated in this connection that
no doubt could have successfully maintained
against the taxpayer to recover their part of th
ship income had he attempted to take or receive
own. Further, it was observed that a curious
would be presented if the taxpayer were requi
count for and pay a tax upon income which h
right to receive and which right existed solely
clusively in the trusts. Accordingly it was held
conclusion of the Tax Court that no valid p
existed for federal income tax purposes was wi

APPLICATION OF THE ABOVE STATED
CIPLES OF LAW TO THE FOLLOWING CIR-
TANCES IN THIS CASE WHICH ARE WITH-
CONTRADICTION IN THE RECORD, COM-
THE CONCLUSION IN THIS CASE THAT
E WAS A REAL INTENT TO CARRY ON THE
NESS AS A PARTNERSHIP.

r. Toor had operated the same business as a
rtnership with his father-in-law as a limited
ack in 1935.

e prime motive for the trusts and the limited
p was something other than tax saving; the
as to make effective provision for the children
possible benefit to Mr. and Mrs. Toor.

e bank and its personnel were strangers to
and dealt at arm's length with him, the bank
s own decisions based on its own investigations.
s no evidence that the bank was a mere tool
oor.

e partnership agreement was properly executed
respects and to all intents and purposes was
nited partnership agreement in accordance with
ne business was set up and conducted as a part-

e economic relation of the parties were changed
or's position as a general partner was substan-
erent from that of sole proprietor

(b) Accountings had to be rendered.

(c) He was subject to the limitations gations imposed by law for limited partner the bank had corresponding rights and pow

(d) Income earned in the business by irrevocably belonged to them, and Mr. T not use it for personal purposes.

(e) Mr. Toor could not make a distri profits to himself without making a pro distribution to the trusts.

(f) The business involved a risk of loss gain, and losses would be shared in prop the extent of the capital investment; profits no means assured at that time.

(6) The business was conducted in accorda the agreement, and Mr. Toor respected the respo and obligations imposed upon him.

(7) Capital and the existing organization at were the major factors in the production of in the trusts had paid for and owned their pro share therein. To the extent Mr. Toor's se counted for income, he was specially compen such services by a reasonable salary in additi share of the profits. This salary was not fou unreasonable and all of the evidence showed

ly over what Mr. Toor had been making for
y and profits for the years prior to the war; a
executive could have been obtained to perform
functions for the same rate of compensation;
was fixed in 1942 when, in an ordinary com-
nture, the amounts received by Mr. Toor would
considered adequate compensation for a com-
cutive; the business ran without Mr. Toor be-
a good part of the time; the large profits were
e result of the war years and having available
, equipment and organization for the production

e bank at all times observed its duties as trustee
cted the interests of the trusts as limited part-

) The bank reviewed the reports received, was
ied thereby, was satisfied as to the integrity and
ct of Mr. Toor and was kept informed by him
the conduct of the business.

) The bank was at all times aware of its rights
limited partner.

) There is no instance in the record where the
was lax in its duties or failed to take any ac-
hat would normally be expected from a limited
er, if this were a partnership with strangers.

suspicion, interference, investigation, crit
for that matter, even the tendering of ad
limited partner not experienced in the busi

(e) There is no evidence that the ban
fully intend to live up to its duties as trus
protect the interests of the limited partners

(9) Once the partnership was established,
benefits that could go to the trusts actually wer
trusts. There were no rebates, kickbacks or an
of a mere paper allocation.

(10) Neither Mr. Toor nor Mrs. Toor cou
benefit from the income earned by the trusts.
the income was used to satisfy their obligation
or otherwise used for their benefit.

(11) There is no evidence in any respect of
on the part of any of the parties.

(12) The parties did join together in good
conduct the business, and agreed that the cap
contributed by each was of such value to the p
that the contributors should participate proporti
the distribution of profits.

III.

rical Error in Omitting the Irrevocability se From the Trust Instruments Did Not Re- in Causing Income From the Partnership to Attributed to Mr. and Mrs. Toor or Justify Disregard of the Fiscal Year of the Partner- for Tax Purposes.

st note that the argument under this point as- partnership is found to be valid. Furthermore, ıe involved under this point of the argument is ated to the partnership for the fiscal year end- 30, 1943.

A. THE FACTS.

idence was without contradiction that it was intended by all parties concerned that the trusts be irrevocable, and it was understood by the ıereof that the Declarations of Trust so stated. ssity that the trusts be irrevocable was discussed and Mrs. Toor by their attorney, Max Fink, t with their approval. Mr. Toor was also spe- dvised by a certified public accountant to make irrevocable. The matter of irrevocability was ıssed with the bank. The first drafts of the ruments contained an irrevocability clause, and parties noted that clause in those drafts. The s went through several draft stages, and in the

trust documents were executed with all of th
under the impression that they contained the irre
clause. [R. 99, 100, 113, 296-306, 320-323,
Exs. 18 and 19].

That there was any question as to irrevoca
first discovered when the bank received a let
September 29, 1943, from the State of Californ
troller's Office, pointing out that there was pr
inadvertent omission of the usual irrevocabili
This letter was in reference to the gift tax ret
mitted to the State of California with the tru
ments as supporting documents. The letter w
mitted to Mr. Fink, who considered what actio
in order to correct the error, and consulted oth
it. Reformation by lawsuit or by agreement
sidered, and the latter course was finally chosen
336, 306-309, 324-326, 174-180, Exs. 20 and
instruments dated December 14, 1943, which w
ized by the bank on January 13, 1944, it was
and confirmed by the trustees and by Mr. and M
that it was the original intention of the partie
trust instruments be irrevocable and that tho
ments were irrevocable [Ex. 14, R. 176-180].

The above facts are not in dispute. The only
is when the trusts should be deemed irrevocable

INTENTION OF THE PARTIES ALWAYS
THAT THE TRUSTS BE IRREVOCABLE AND
TRUSTS SHOULD BE VIEWED ACCORD-
Y. THE REFORMATORY INSTRUMENTS OF
MBER 14, 1943, IN ANY EVENT, SHOULD BE
IDERED TO BE RETROACTIVE TO THE
WHEN THE CLERICAL ERROR OCCURRED.

ne error was a mere inadvertent clerical one is
spute. The documents were not the ones the
tended to execute. The money was delivered
nk and accepted by it irrevocably. This is not
n such as was presented in *Gaylord v. Commis-*
th Cir., 1946), 153 F. 2d 408, where the docu-
the one the taxpayer intended to sign, but be-
a mistake as to its legal effect, it failed to
his later claimed "intention" and "desire."

role evidence rule, as well as special statutory
on thereof has its well established exceptions
rough mistake, accident or imperfection in the
he written document does not contain the true
ng of the parties.

lifornia Code of Civil Procedure, Section 1856;
lifornia Civil Code, Section 1640.

t mentioned section provides that:
When, through fraud, mistake, or accident, a writ-
ontract fails to express the real intention of the
such intention is to be regarded, and the erro-

Contracts may be revised or reformed to reflec
agreement of the parties, notwithstanding th
States government is a party, and notwithstandi
quirements of statute or the Statute of Frauds.

See:

Ackerlind v. United States, 240 U. S. 53
Ct. 438, 60 L. Ed. 78, and cases cited

So, too, in tax cases a taxpayer is not conclusiv
for tax consequences by a written contract whi
executed, where such contract does not reflect
situation.

See:

Arthur R. Jones Syndicate v. Commissi
Cir., 1927), 23 F. 2d 833.

This right to correct a mistake applies to any
defect in a written contract whether it is in re
common law or statutory requisite.

45 Am. Jur. 601;

22 Cal. Jur. 709.

A contract may be reformed by adding an omi
lation.

Fresno Canal & Irrigation Co. v. Hart
453, 92 Pac. 1010 (1907);

22 Cal. Jur. 715.

ıay reform it voluntarily as effectively as if the
ɔn were decreed in an action in equity.
Am. Jur. 637;
A. L. R. 119.

instant case, reformation was not sought from
court nor was an attempt made in any way to
ıe action into one for reformation. Plaintiff
that the true original intent should have been
and in any event, the original instruments had
een reformed by documents executed on Decem-
943. We did not assert that such contention or
reformation would be conclusive on the govern-
the government was, of course, free to attack
ty of the statement of the true original intent
e reformatory instruments. This they did not
ıpt to do. Whether the true original intent was
l or whether the voluntary reformation accom-
ı December 14, 1943, was valid and effective,
sue in this case and properly before the Court.
er of fact, this was the first opportunity for the
to litigate this question with the government.
ɔt necessary that a court reformation be first
ɔefore the trial court in this case could recognize
riginal intent or the effectiveness of the reforma-
ıments. (See Civil Code, California, Sec. 1640.)
formation effected by the instruments should be

give the voluntary reformation the same effect
decree, which would be a proper result. Upon the
tion of an instrument, the rule is that it relate
and takes effect from the time of its original
especially as between the parties thereto and a
tors at large and purchasers with notice.

45 Am. Jur. 591.

Certainly, the government cannot assert that
prejudice or injury would result to it from accord
active effect to the correction of the clerical erro
respect, the government is not in the position
fide purchaser for value who has acquired rights
of the parties to the instrument sought to be ref

Cf. Baines v. Zuibeck (1948), 84 Cal
483, 191 P. 2d 67.

The government was never misled on accou
mistake in the slightest degree. On the contrar
information the government received would be
tax returns filed shortly after the creation of
and by these returns the government was notifie
trusts were irrevocable (pp. 332-333).

If Mr. Toor, prior to December 14, 1943
covered the error and attempted to revoke the
would have been the bank's duty as trustee to
revocation, to sue for reformation and reforma
have been granted. It cannot be assumed that
would not perform its duties as trustee. In
Mr. and Mrs. Toor did not have the actual po
voke the trusts and this further distinguishes th

IF NOT GIVEN RETROACTIVE EFFECT, CORRECTION OF THE CLERICAL ERROR ACCOMPLISHED ON DECEMBER 14, 1943, ER THAN ON JANUARY 13, 1944, AS FOUND HE COURT. THIS CORRECTION WAS AC- LISHED WITHIN THE CALENDAR TAX- YEAR OF MR. AND MRS. TOOR AND OF TRUSTS AND PRIOR TO THE TIME THE RNMENT'S RIGHTS HAD ACCRUED.

14 was as follows [R. 70]:

ne trust instruments contain no statement that vere not revocable by the grantors. It was not January 13, 1944, that there were executed lments to the trust instruments which stated hey were not so revocable."

ding is definitely without support in the evi- he only evidence is in the instruments them- ich state that they were executed on the date December 14, 1943 [Ex. 14; R. 177, 179]. The he officers of the bank acknowledged their sig- a later date is in no way contradictory of this t support the Court's finding. As a matter of cknowledgment was not even required for the to be effective.

he Federal income tax laws, profits accruing to hip during its fiscal year are not distributable nbers of such partnership until the last day of ear of the partnership, at which time they are l or become ascertainable.

in the case of an individual . . ." Sectio
vides in part that "the net income shall be comp
the basis of the taxpayer's annual accounting (
or calendar year as the case may be) . . ." I
182, each partner, in computing his net inco
quired to include his distributive share of the
income of the partnership, as computed by th
ship under Section 183.

The fiscal year of the partnership ended on J
each year, the first fiscal year ending June 30, 1
and Mrs. Toor and the trusts were each on a
year basis. Under these circumstances, Sectio
the Internal Revenue Code becomes applicable,
section provides:

> "If the taxable year of a partner is diffe
> that of the partnership, the inclusions wi
> to the net income of the partnership, in
> the net income of the partner for his tax
> shall be based upon the net income of the p
> for any taxable year of the partnership
> beginning on, before, or after January 1, 1
> ing within or with the taxable year of the

Accordingly, any net income accruing to th
ship during the first fiscal year, would not hav
cludable as income in the returns of the partne
calendar year 1942, but would necessarily have
cluded as income in their calendar taxable ye
December 31, 1943.

Section 166 of the Internal Revenue Code pro

166 is an exception to the general rule that in-
xable to the recipient, and said section must be
nstrued.

rton's Law of Federal Taxation, Vol. 6, p. 410.

ute does not provide that the trust as an entity
isregarded, nor does it require that a partner-
hich such trust might be a member, must be
d. The trust as well as the partnership are
ve, and the fiscal year adopted by the partner-
be recognized. In this connection see *Hash v.*
ner (1945), 4 T. C. 878 (aff'd. 4th Cir., 152
2), wherein the Court refused to permit the
ner to disregard the fiscal years set up by the
p agreements to which the trustees were parties,
nding that the taxpayers were chargeable with
on the income from the trusts.

r. and Mrs. Toor were on a calendar basis, and
the trusts were held revocable, the income accru-
the partnership to the trusts at the close of the
p fiscal year ending June 30, 1943, would have
included by them in computing their net in-
the calendar year ending December 31, 1943.
the rights of the government from a tax lia-
dpoint did not accrue until the close of the taxa-
to wit, December 31, 1943, and since the cor-
the clerical error was accomplished on Decem-
the government is not entitled to complain of
tion of such clerical error; Mr. and Mrs. Toor

The right to make corrections and adjustm
to the close of a taxable year has been clearly
by numerous decisions.

Huntington-Redondo Company v. Com
(1937), 36 B. T. A. 116;

Albert W. Russell v. Commissioner, 35
602.

D. THE SAME GOVERNMENT ACCEPTED
NEE'S RETURN MADE SHORTLY AFT
CREATION OF THE TRUSTS ON AN IR
BLE BASIS; THE SAME GOVERNM
RENEGOTIATING WAR CONTRACTS, DE
AND RECEIVED SOME $60,000 BASED
RECOGNITION OF THE PARTNERSHIP
FISCAL YEAR WHICH COULD NOT OTH
HAVE BEEN ASSESSED OR COLLECTED

1. Shortly after the creation of the trusts
gift tax returns were filed and accepted by th
ment on an irrevocable basis [R. 332-334].

2. As heretofore pointed out, a change in th
tiation law increased the amount of exemption
negotiation of persons, firms or corporations w
able year ended after June 30, 1943. Since th
ship's fiscal year ended June 30, 1943, it could
advantage of this increased exemption. If the
ship were not in effect, Mr. Toor could have
vantage of this increased exemption. By recog
partnership and its fiscal year, the government
able to renegotiate government contracts of th

regoing discussion has been directed to the in-
uing from the partnership at the close of the
· ending June 30, 1943. The income accruing
30, 1944, for the previous fiscal year, and on
1945, for the previous fiscal year, of course,
) the trusts after the trusts had unquestionably
e revocable. Such income would thus not be
) Mr. and Mrs. Toor in any event.

Conclusion.

ue respect to the learned Trial Court, it is sub-
at the decision in the instant case violates the
tal precept of income tax law, that income shall
to he who earns it. This principle is broken
) two further basic principles, one, that income
perty is attributable to the owner of the prop-
two, that income from personal services is at-
to the person rendering the services. There
son for applying different principles to partner-
ne. If an individual makes a bona fide gift of
e or of a share of capital stock, the rent or
ncome is taxable to the donee. Similarly, how-
owner of a partnership interest may have ac-
ch interest, the income is taxable to him for he
l owner.

instant case, the personal services of Mr. Toor
pensated for by a reasonable salary. The bal-
ne income from the business was earned by the
and the trusts were each a one-sixth owner of

first place, the situation is like that of a father
up a trust for his son by way of gift, and
the trust purchases real property. If the gift is
father is not taxed on the income even if he ac
the property for the benefit of the child. In t
place, the control of Mr. Toor was no more tha
a general partner in an ordinary limited pa
Furthermore, in weighing the effect of the ret
power upon the *bona fides* of a purported gift o
power exercisable for the benefit of others mu
tinguished from the power vested in a transfero
own benefit. To hold that the extent of contro
business in the instant case was such as to ch
Toor with earning the entire income therefrom i
tical effect to rule that a family limited partn
invalid for tax purposes where original capital is
tributed by the limited partners. The Trial C
has taken a limited partnership, otherwise valid
effect, ruled it invalid for tax purposes becau
existence of a family relationship.

In this case, there is no question as to the re
bona fides of the gift to the trusts. The trust
and beneficially acquired an ownership in the bu
the investment of a proportionate amount of cap
in, regardless of the fact that the capital orig
way of gift. There was no evidence of bad fa
soever and all of the evidence pointed to the g
of the parties. There was no substantial eviden
otherwise than that the parties joined together
faith to conduct a business, having agreed that t

bmitted that the decision of the Trial Court has a result whereby the taxpayer is required to or and pay a tax upon income which he had no receive, enjoy, or benefit from, but which right clusively in the trusts. By a ruling and unsupdings which indicate "at best an error in emhe Trial Court has judicially legislated the famd partnership formed with gift capital into a In this case, it is clear that Mr. Toor intended his particular gift to the trusts to $21,000; inwould be forced by this decision to pay in adne $200,000, without receiving or being entitled income upon which it is based. Under all the , this result is unjust and contrary to law.

cision of the Trial Court should therefore be insofar as it concerns the ruling that the partas not valid for tax purposes. It should further that the trusts should be considered irrevocable r inception, that the fiscal year of the partnerld not have been disregarded and that the inibuted to the trusts from their partnership inere erroneously attributed to Mr. and Mrs. Toor the years in question.

Respectfully submitted,

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LEO V. SILVERSTEIN,
SCHWARTZ, GALE & BLOOM,
Attorneys for Appellants.

ations Code of California:

5509. Rights, Powers and Liabilities of a Partner. (1) A general partner shall have ghts and powers and be subject to all the re- and liabilities of a partner in a partnership imited partners, except that without the written r ratification of the specific act by all the limited a general partner or all of the general partners authority to:

o any act in contravention of the certificate.

o any act which would make it impossible to the ordinary business of the partnership.

onfess a judgment against the partnership.

ossess partnership property, or assign their rights c partnership property, for other than a partner- pose.

dmit a person as a general partner.

dmit a person as a limited partner, unless the to do is given in the certificate.

ontinue the business with partnership property eath, retirement or insanity of a general part- ss the right so to do is given in the certificate.

5510. Rights of Limited Partner. (1) A artner shall have the same rights as a general o

ave the partnership books kept at the principal

partnership affairs whenever circumstances ren
and reasonable; and

(c) Have dissolution and winding up by
court.

(2) A limited partner shall have the right
a share of the profits or other compensation b
income, and to the return of his contribution a
in Sections 15515 and 15516.

Sec. 15523. Distribution of Assets. (1
tling accounts after dissolution the liabilities of
nership shall be entitled to payment in the
order:

(a) Those to creditors, in the order of p
provided by law, except those to limited partn
count of their contributions, and to general p

(b) Those to limited partners in respect to t
of the profits and other compensation by way
on their contributions.

(c) Those to limited partners in respect to
of their contributions.

(d) Those to general partners other than
and profits.

(e) Those to general partners in respect to

(f) Those to general partners in respect to

(2) Subject to any statement in the certifi
subsequent agreement, limited partners share in
nership assets in respect to their claims for c
in respect to their claims for profits or for co